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IN THE

Supreme Court of the United States

No. 208

ASSOCIATED STORES, INC.,
Petitioner

v.

INDUSTRIAL LOAN AND INVESTMENT COMPANY
Respondent

RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI

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OBJECTIONS TO JURISDICTIONAL GROUNDS

The respondent contends there are no special and important reasons for a review on writ of certiorari under Supreme Court Rule 19 in this case. Pertaining to the points in this petition, the decision of the Court of Appeals for the Fourth Circuit in affirming the judgment below is not in conflict with decisions of other Courts of Appeals, as this is a diversity action calling only for the construction of a North Carolina statute. The decision is not in conflict with applicable and controlling state decisions. Furthermore, a change in the applicable statutory law after this action was begun, which does not apply to this action, has rendered the petitioner's second question a matter of concern

only between the petitioner and respondent and the question is no longer a matter of public concern.

Counsel for petitioner fully and freely agreed for the case to be heard in the absence of Judge Haynsworth, after being apprised that if either counsel objected to the absence of Judge Haynsworth, the arguments would be rescheduled for hearing at a later date. The Court of Appeals for the Fourth Circuit did not depart from the accepted and usual course of judicial proceedings in its handling of this matter.

STATUTES

"G. S. 24-2. Penalty for usury; corporate bonds may be sold before par. The taking, receiving, reserving or charging a greater rate of interest than six per centum per annum, either before or after the interest may accrue, when knowingly done, shall be a forfeiture of the entire interest which the note or other evidence of debt carries with it, or which has been agreed to be paid thereon. And in case a greater rate of interest has been paid, the person or his legal representatives or corporation by whom it has been paid, may recover back twice the amount of interest paid in an action in the nature of action for debt. In any action brought in any court of competent jurisdiction to recover upon any such note or other evidence of debt, it is lawful for the party against whom the action is brought to plead as a counterclaim the penalty above provided for, to wit, twice the amount of interest paid as aforesaid, and also the forfeiture of the entire interest. If security has been given for an usurious loan and the debtor or other person having an interest in the security seeks relief against the enforcement of the security or seeks any other affirmative relief, the debtor or other person having an interest in the security shall not be required to pay or to offer to pay the principal plus legal interest as a condition to ob-

taining the relief sought but shall be entitled to the advantages provided in this section. Nothing contained in this section or in Sec. 24-1, however, shall be held or construed to prohibit private corporations from paying a commission on or for the sale of their coupon bonds, nor from selling such bonds for less than the par value thereof: nor shall anything contained in this section or in Sub-Sec. 24-1 and 24-3 be held or construed to prohibit private corporations from making contracts, incurring liabilities, borrowing money and paying a charge therefor not exceeding six per centum (6%) of the original amount of the loan for each twelve (12) months of the duration of the same, notwithstanding that such loan is payable in installments. (1876-7, c. 91; Code, S.3836; 1895, c. 69; 1903, c. 154; Rev., s. 1951; C. S., s. 2306; 1955, c. 1196; 1959, c. 110.)"

Found in General Statutes of North Carolina, Vol. 1C, 1963 Cumulative Pocket Supplement, page 286.

The fourth sentence of this statute was inserted in 1959 by 1959 Session Laws, Chapter 110, page 90, which reads as follows:

"AN ACT TO AMEND G. S. 24-2 SO AS TO MAKE ITS PROVISIONS APPLY WHERE A DEBTOR OR OTHER PERSON SEEKS EQUITABLE RELIEF.

"The General Assembly of North Carolina do enact:

"SECTION 1. G. S. 24-2 is hereby amended by inserting immediately following the third sentence thereof the following new sentence:

'If security has been given for an usurious loan and the debtor or other person having an interest in the security seeks relief against the enforcement of the security or seeks any other affirmative relief, the debtor or other person having an interest in the security shall

not be required to pay or to offer to pay the principal plus legal interest as a condition to obtaining the relief sought but shall be entitled to the advantages provided in this Section.'

"SECTION 2. All laws and clauses of laws in conflict with this Act are hereby repealed.

"SECTION 3. This Act shall become effective July 1, 1959.

"In the General Assembly read three times and ratified, this the 24th day of March, 1959."

STATEMENT OF CASE

This action was begun by petitioner against respondent under N. C. G. S. 24-2 in December, 1957, in the Superior Court of Wake County, North Carolina and was removed by respondent to the United States District Court for the Eastern District of North Carolina on the ground of diversity of citizenship and the amount involved under 28 U.S.C.A. 1332.

Petitioner and respondent had entered into two contracts referred to as the "1955 Master Contract" (Report of Special Master, paragraph 7, Petitioner's Appendix, pages 4-7) and the "1956 Master Contract", (Report of Special Master, paragraph 19, Petitioner's Appendix, pages 9-13). Petitioner was in the business of selling sewing machines on time prices secured by conditional sales contracts. Under the above Master Contracts the petitioner discounted and assigned to respondent these contracts at eleven (11%) per cent discount, with petitioner guaranteeing payment of the assigned conditional sales contracts. These transactions, because of the guaranty of payment, were held to be loans by the District Court and the Court of Appeals for the Fourth Circuit.

The points in this petition for writ of certiorari deal only with conditional sales contracts outstanding at the institution of the action and as all conditional sales contracts assigned under the "1955 Master Contract" had been paid, we are concerned only with the "1956 Master Contract". As to the assigned contracts that had been paid, petitioner secured in this action the exact relief he sought, to wit, twice the amount of interest paid.

Petitioner, upon institution of the action, asked that the respondent be restrained from collecting from the makers of the conditional sales contracts assigned to respondent and that respondent be required to forfeit all interest outstanding as the rate was usurious. The restraining order was allowed by the Wake County Superior Court on December 18, 1957. Report of Special Master, paragraph 52, Petitioner's Appendix, page 21. The restraining order was returnable on January 5, 1958, but since the action was removed to the United States District Court for the Eastern District of North Carolina by reason of diversity and the amount involved, the return order was heard on January 6, 1958, by United States District Judge Don Gilliam. By order of February 4, 1958, Judge Gilliam dissolved the restraining order of the Wake County Superior Court and awarded collections to the respondent until further order of the Court. Report of Special Master, paragraph 53, Petitioner's Appendix, page 23.

As to the points in this petition, the District Court held that Judge Gilliam's order allowing the respondent to make collections until further order of the Court did not relieve petitioner of its obligation to the respondent for any uncollectible balance due on the outstanding conditional sales contracts and that petitioner by seeking equitable relief to have the usurious element of his debt eliminated must do equity and pay the principal plus interest at the legal rate of six (6%) per cent under the applicable decisions of North Carolina. The decision of the District Court was affirmed by the Court of Appeals for the Fourth Circuit.

ARGUMENT

The petitioner states as a reason for review on writ of certiorari that the decision is in conflict with decisions of other Courts of Appeal. As stated above, this action was instituted in the Wake County, North Carolina Superior Court under North Carolina General Statutes 24-2 and was removed to the United States District Court for the Eastern District of North Carolina by the respondent on the grounds of diversity of citizenship and the amount involved. The legal question involved is a construction of G. S. 24-2 and the North Carolina decisions construing this statute. There are no decisions of other Courts of Appeal construing the North Carolina statute so there can be no conflict of decisions between Courts of Appeal as argued by petitioner. Petitioner in its brief cites only one case from another Court of Appeals, that being *Chandler v. McKerral*, 68 F. 2d 343, (9th C.C.A. 1934) cited at page 8. The *Chandler* case deals with the fraudulent sale of stock by a corporation and does not in any way involve usury or G. S. 24-2, and the decisions of the North Carolina Supreme Court.

FIRST QUESTION

The petitioner poses the following question:

Did the Court below err in failing to hold that any liability or obligation of petitioner to respondent was paid, satisfied or discharged in full with respect to any balance outstanding on any conditional sales contracts, the collection upon which was awarded to respondent by order of Gilliam, District Judge, dated February 4, 1958?

The petitioner purports to make two points in support of its position:

1. That any liability or obligation of petitioner to respondent was paid, satisfied or discharged by the order entered by Judge Gilliam on February 4, 1958.

2. That the efforts of respondent in making collections pursuant to said order of Judge Gilliam were so inadequate as to relieve petitioner of liability as guarantor on the outstanding contracts which it was collecting pursuant to Judge Gilliam's order, and that the Special Master should have so found.

The petitioner instituted this action and requested, among other relief that the complaint be treated as an affidavit and petition for equitable relief, that the court issue a temporary restraining order enjoining the respondent from securing the payment of the balances due by makers of conditional sales contracts; that upon the show-cause hearing, the temporary injunction be continued until the trial at which time the petitioner would pray that the temporary restraining order be made permanent.

The Honorable William Y. Bickett, Judge of the Superior Court of Wake County, upon the complaint, issued a temporary restraining order and directed the respondent to appear on January 5, 1958, to show cause, if any it had, why the order should not be continued until the trial of the case on its merits. The case was removed to the United States District Court and this hearing was held by Gilliam, District Judge. Judge Gilliam in his order entered on February 4, 1958, dismissed the temporary restraining order against the respondent and directed that the respondent proceed with the collection of the payments on the conditional sales contracts held by it. Judge Gilliam made no decision as to the final rights of the parties and made the following entry:

> "4. That this order is effective as of the opening of business February 5, 1958, and only until the further orders of the Court and the findings herein are based upon prima facie conclusions only." Petitioner's Appendix page 27.

As stated above the law of the case is that the discounting of the conditional sales contracts with a guaranty constitutes

a series of loans, the guaranty being the controlling factor in the decision. The transactions being loans, the assignment of the conditional sales contracts simply created security for the loans. Petitioner in asserting that Judge Gilliam's order allowing respondent to make collections from the makers of the conditional sales contracts relieved petitioner of its obligation on its guaranty of payment of the conditional sales contracts misses the whole point. Petitioner attempts to assert the principle of equitable estoppel in that respondent in asking to make collection after petitioner had restrained respondent from doing so and then seeking to recover the balance due on uncollectible conditional sales contracts took inconsistent positions. Respondent submits that the only inconsistent position taken in this action is that of the petitioner in relying upon the guaranty of payment to convert the transactions into loans and now asserting the order allowing respondent to collect directly from the makers of the conditional sales contract relieves it of its obligation on the guaranty.

In addition, the Court's attention is directed to the right given to the respondent by the petitioner in paragraph 15 of the 1956 Master Contract, Report of Special Master, paragraph 19, Petitioner's Appendix, page 12, which reads as follows:

> "15. First Party, may, at its option, should it appear advisable to it, and in order to protect its interest in the money advanced by it; in case of financial difficulties or otherwise of said Second Party, notify all contract obligors to remit direct to it, the unpaid balances of any and all contracts held by said First Party."

In short, petitioner's contention is that if a secured creditor collects on the security he is barred from collecting any deficiency from the debtor, which is obviously without merit. The Court's attention is invited to the rules of law laid down in the following two cases: *Rierson v. Hanson*, 211 N. C. 203,

189 S. E. 502 (1936) where the "Bankruptcy Rule" was applied, held a creditor having collateral security is allowed to prove the balance of his claim only after exhausting the collateral security. *Bank v. Jarrett,* 195 N.C. 798, 143 S.E. 827 (1928) where the "Chancery Rule" was applied, held a secured creditor could share in the general fund before resorting to the security. Regardless of which rule is applied, neither prevents the creditor from recovering a deficiency from the debtor. The attention of the Court is invited to Judge Craven's opinion on this point in Petitioner's Appendix, page 50.

The petitioner further contends that efforts of the defendant in making collections pursuant to the order of Judge Gilliam were so inadequate as to relieve the plaintiff of liability as guarantor on the outstanding contracts which it was collecting pursuant to Judge Gilliam's order, and that the Special Master should have so found. Judge Craven said on this point,

> "To be sure Industrial had a duty to exercise reasonable diligence in attempting to collect upon individual customer contracts so as to mitigate and diminish its claim against Associated. I do not construe the Findings of Fact to require a conclusion of law that Industrial failed to perform this duty, and I overrule Associated's objection to the failure of the Special Master to so find."
>
> *Associated Stores, Inc. v. Industrial Loan and Investment Company,* 202 F. Supp. 251 (1962). Petitioner's Appendix, page 51.

This conclusion is well supported by the evidence and is a determination of fact rather than law.

SECOND QUESTION

The petitioner poses as its second question the following:

Did the Court below err in determining that petitioner had sought equitable relief in such fashion as to mitigate the effect

of the North Carolina usury law (G. S. 24-2) as applied to a portion of the unlawful interest exacted of petitioner by respondent?

As pointed out previously in this brief, petitioner upon the institution of this action, sought and received a temporary restraining order against respondent, thus invoking the equitable jurisdiction of the Court. When the cause came on to be heard upon the return date of the order, the restraining order was dissolved. The attention of the Court is invited to the fact that this point applies only to the outstanding conditional sales contracts at the date the action was instituted. It in no way concerns the conditional sales contracts that had been paid in full or any interest paid on those contracts. Thus the only provision of the North Carolina usury law (G. S, 24-2) that is before the Court on this point is the provision relating to forfeiture of all interest if the rate is usurious.

Respondent submits that the law of North Carolina, discussed below, at the time this action was instituted, clearly sets forth that a debtor who goes into court seeking equitable relief from an executory contract that he claims is usurious must as a condition of relief pay the principal plus the legal rate of interest under the principle that "he who seeks equity must do equity". The Special Master, the District Court, and the Court of Appeals for the Fourth Circuit, so found the law to be, and held that petitioner, as a debtor who had sought equitable relief as to the debt, must first pay the principal and the legal rate of interest before being entitled to any relief as to any indebtedness arising from any outstanding conditional sales contract.

The law that a debtor who seeks to restrain the collection of an usurious debt on an executory contract is not entitled to a complete forfeiture of all the interest but must pay the principal plus the legal rate of interest is clearly set forth in the landmark case of *Waters vs. Garris*, 188 N.C. 305, 124 S.E. 334 (1924):

"It is the established law of this jurisdiction that when a debtor, who has given a mortgage to secure the payment of a loan, comes into equity, seeking to restrain a threatened foreclosure under the power of sale in his mortgage, as a deliverance from the execution of usury, he will be granted relief and allowed to have the usurious charges eliminated from his debt only upon paying or tendering the principal sum with interest at the legal rate, the only forfeiture which he may thus enforce being the excess of the legal rate of interest. *Corey vs. Hooker*, 171 N.C. 229; *Owens vs. Wright*, 161 N.C. 127. This ruling which has been established by an unbroken line of precedents, beginning with *Taylor vs. Smith*, 9 N.C. 465, and running through a multitude of cases down to our latest decision in *Adams vs. Bank*, 187 N.C. 343, is based upon the principle that he who seeks equity must do equity. It is a well recognized rule of equity jurisprudence that one, who seeks the aid of a court of equity to be relieved from usury, must do equity by paying or offering to pay the principal sum borrowed, with lawful interest thereon, as a condition precedent to the granting of the relief sought. 39 Cyc., 1010.

"The following clear and succinct statement of the doctrine is taken from 27 R.C.L., 264: 'It is well settled, in the absence of statutes to the contrary, that one seeking relief in a court of equity from a usurious contract must, as a condition of relief, do everything that equity requires, and if a borrower goes into a court of equity, in respect to a security given in connection with usurious contracts, or to avoid extortion or oppression, the court will compel him to pay principal and legal interest if the contract is executory, because there is moral obligation resting on him to do so, and it is equitable that he should be compelled to do it. The rule of course rests on the maxim that 'he who seeks equity must do equity'."

In *Bailey v. Inman*, 224 N.C. 571, 31 S.E. 2d 769 (1944) the Court said:

> "The principle is well settled by numerous decisions of this Court that where a debtor seeks the aid of a court of equity on the ground that his debt is tainted with usury, he may have the usurious element, if any, eliminated from his debt only upon his paying the principal of his debt with interest at the legal rate. In such case he is not entitled to the benefit of the statutory penalties for usury. Connor, J., in *Smith v. Bryant*, 209 N.C., 213, 183 S.E., 276. See also *Waters v. Garris*, 188 N.C., 305, 124 S.E., 334; *Miller v. Dunn*, 188 N.C. 397, 124 S.E., 746; *Jonas v. Mortgage Co.*, 205 N.C., 89, 170 S.E., 127; *Mortgage Co. v. Wilson*, 205 N.C., 493, 171 S.E., 783; *Kenny v. Hotel Co.*, 208 N.C., 295, 180 S.E., 697; *Buchanan v. Mortgage Co.*, 213 N.C., 247, 195 S.E., 787."

For a collection of the cases see Annotations in 135 A.L.R. 808 (1941) and 166 A.L.R. 459 (1947).

While the North Carolina Supreme Court has expressed some concern with this rule of law, the Court has nevertheless recognized and applied it where the debtor seeks equitable relief.

Smith v. Bryant, 209 N.C. 213, 183 S.E. 276 (1935).

Indeed, the rule was so imbedded in the law of North Carolina by the cases at the time this action was instituted, the General Assembly in 1959 enacted an amendment to G. S. 24-2 in order to change it. (1959 Session Laws, Chapter 110, *supra*, page 3.)

This amendment which became effective July 1, 1959, while not applicable to this action, renders this question a matter of concern only to the parties to this action and it is no longer a matter of public importance. In *Rice v. Sioux City Memorial Park Cemetery*, 348 U.S. 880, 75 Sup. Ct. 122, 99 L.Ed. 693

(1954), Writ of Certiorari was issued to the Supreme Court of Iowa. Petitioner there had sought damages to compensate her for mental suffering claimed to flow from defendant cemetery's refusal to bury her husband, a Winnebago Indian, because the contract of sale of the burial lot provided that "burial privileges accrue only to members of the Caucasian race." On petition for rehearing in 349 U.S. 70, 75 Sup. Ct. 614, 99 L. Ed. 897 (1955) the Writ of Certiorari was dismissed when the Court discovered that after commencement of the action, Iowa enacted a statute which prohibited cemeteries from denying burial on account of race or color, declared racial restrictive covenants in burial contracts void, and by implication, allowed an injured party to recover damages in a civil action based on a violation of the statute. Justice Frankfurter speaking for the majority said at 349 U.S. 76, 99 L.Ed. 902:

> "Had the statute been properly brought to our attention and the case thereby put into proper focus, the case would have assumed such an isolated significance that it would hardly have been brought here in the first instance."

and at 349 U.S. 79, 99 L.Ed. 904,

> "If it be suggested that as much effort and time as we have given to the consideration of the alleged conflict would have enabled us to dispose of the case before us on the merits, the answer is that it is very important that we be consistent in not granting the writ of certiorari except in cases involving principles, the settlement of which is of importance to the public as distinguished from that of the parties, and in cases where there is a real and embarrassing conflict of opinion and authority between the circuit courts of appeal."

CONCLUSION

The respondent submits that this petition presents no special important reasons for a review on writ of certiorari.

Respectfully,

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